
**IN THE HIGH COURT OF PUNJAB AND HARYANA AT
CHANDIGARH**

I.T.R. No.174 of 1989

Date of decision: 26.3.2007

The Commissioner of Income-Tax, Amritsar ...Petitioner

Versus

M/S Amrik Singh Surinder Singh, Amritsar ...Respondent

**CORAM: HON'BLE MR.JUSTICE M.M.KUMAR
HON'BLE MR.JUSTICE RAJESH BINDAL**

Present: Mr.Sanjiv Bansal, Advocate for the Revenue

RAJESH BINDAL, J.

Following questions of law have been referred for opinion of this Court by the Income Tax Appellate Tribunal, Amritsar Bench, Amritsar (for short, 'the Tribunal) arising out of its order dated 5.12.1980 in ITA No.592(ASR)/1979 for the assessment year 1975-76:-

- “1. Whether on the facts and in the circumstances of the case, while rightly affirming the order of the CIT (A) rejecting the assessee's claim of deduction of Rs.4,15,944/- as bad debt under section 36 (2) of the Income Tax Act, 1961, the Appellate Tribunal is right in law in allowing the same as trading loss incurred by the firm under section 37 of the Act?
2. Whether on the facts and in the circumstances of the case, the Appellate Tribunal is right in holding that the agreement dated 1.10.1973 between the Principal M/S Central Distillery & Chemical Works Ltd. and the assessee firm stood modified by the Principal's letter dated 31.10.1973 so as to saddle the assessee firm with the principal's old due from a third party, M/S Nagaland Liquor Stores transforming it as the assessee's own liability towards the

Principal as a trade debt so as to enable the assessee to claim it as its own business liability towards the Principal for the year under consideration?

3. Whether on the facts and in the circumstances of the case the Appellate Tribunal is right in holding that the amount of Rs. 4,15,944/- which was due from the aforesaid third party to the principal long before the agreement dated 1.10.1973 became a trading liability of the assessee firm during the period relevant to assessment year 1975-76 by virtue of the Principal's letter dated 16.5.1974 to the assessee firm?
4. Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in allowing the aforesaid amount of Rs. 4,15,944/- as trading loss in the assessment year 1975-76 despite the un-rebutted finding of the CIT (A) that there was not an iota of evidence brought on the record by the assessee to show that any effort was made to recover these dues from M/S Nagaland Liquor Stores or its partners, one of whom was the son of a partner of the firm? and
5. Whether on the facts and in the circumstances of the case, the finding of the Appellate Tribunal that the amount of Rs. 4,15,944/- was a loss suffered by the assessee firm in the course of running of its business or incidental thereto is vitiated by consideration wholly irrelevant and inadmissible and ignoring of all relevant material on the record?"

Briefly the facts, as noticed by the Tribunal in the statement of case, are that the assessee was a partnership firm working as sole-selling agent of M/s Central Distillery & Chemical Works Ltd. (for short 'the principal') for sale of Indian made foreign liquor. While filing return for the assessment year in question, the assessee claimed bad debt to the tune of Rs. 4,35,243/- in respect of the following constituents:-

1. Rs. 14,500/- Ramesh Films, Gauhati
2. Rs. 4,15,944/- M/S Nagaland Liquor Store, Dhampur,
Nagaland.
3. Rs. 4,622/- Officer Commanding Sikh Light Infantry
Regiment.

4. Rs. 177/- Officer Commanding 235 Rocket Battery.

Rs. 4,35,243/-

The claim made by the assessee was disallowed by the Assessing Officer. The order of Assessing Officer was confirmed in first appeal. In further appeal before the Tribunal, the assessee restricted the claim only in respect of bad debt amounting to Rs. 4,15,944/- in respect of M/S Nagaland Liquor Store, Dhampur, Nagaland and gave up rest of the claim.

Before the Assessing Officer, the assessee raised two contentions, namely: that the amount in question be treated as a debt and since the debt has been written off as unrecoverable, the same being bad debt should be allowed as a deduction. In the alternative, it was pleaded that the amount in question be treated as a trading loss. However, both the pleas were negated by the Assessing Officer. In Appeal before the Commissioner of Income Tax (Appeals) also the order passed by the Assessing Officer was upheld. In further appeal before the Tribunal, the assessee while re-iterated its earlier submissions pleaded that the assessee was working as a sole selling agent of the principal from the assessment year 1967-68. As per terms of the agreement dated October 1, 1973, the assessee was not only responsible for sale of the liquor but also for recovery of dues thereof. In case of failure, the amount was recoverable from the assessee. In return the assessee used to get commission on sales. It is further noticed that M/S Nagaland Liquor Store had been receiving supplies of liquor worth lacs, however, because of change in Government in Nagaland in 1975, licence of M/S Nagaland Liquor Store was not renewed which forced it to close its business. As the amount could not be recovered by the principal in the absence of assets to secure the same, it was debited to the account of the assessee. The assessee referred to and relied upon the clause as agreed to between the principal and the assessee vide letter dated October 31, 1973 to substantiate his claim. The same is extracted below:-

“This is in continuation of our letter of agreement dated 1st

October, 1973.

It is clearly understood that all the out-standings which arise and become due on account of our supplies of liquor to the parties through your agencies and in case that become irrecoverable you will be solely responsible for that and it is in consideration of this that the commission is being paid to your (sic you) as discussed in the agreement Ist Oct., 1973.

So such outstanding which becomes irrecoverable will be recoverable from you which please note.”

The Tribunal though rejected the plea of the assessee to treat the loss as a bad debt but accepted the same as a business loss, while recording the following findings:-

“10. The D.R. on the other hand resisted the contention that the claim could be allowed as a bad debt. He relying on the findings of CIT referred to Para 4(1) and submitted that the principal condition of a claim for bad debt, namely, the amount of claim must have formed a part of the assessed turnover in earlier years. The condition not being fulfilled the claim was drowned out for an ignominious end. As far as the other contention of trading loss is concerned he submitted that the claim was not borne out from facts. Relying on the findings of the CIT he contended that liability of the assessee for outstanding relating to the years prior to the agreement dated Ist October, 1973 was not made out. The letter dated 31st Oct 1973 by the principal which had the effect of modifying the agreement related to outstanding under that agreement and could not relate to earlier years. He submitted that the finding of the CIT was not only correct but also reasonable and did not require any interference.

11. Having heard the rival views and their respective contentions we are not inclined to agree with the contentions of the Revenue and support the findings of the CIT (Appeals). Although we hold that the claim for bad debt raised as an alternative plea by the assessee is not made out in law and is,

therefore, liable to be rejected, we cannot but uphold the claim for trading loss. We agree with the CIT that for a bad debt to succeed the amount of bad debt must have formed a part of the assessed turnover as required under Sec. 36(2). Since the amount had never formed a part of the assessed turnover of the assessee, the amount was not a debt and could not be a bad debt in the hand of the assessee. Therefore, the claim of the assessee for an allowance for bad debt is liable to be rejected. It is only as a business loss the claim is liable to be considered and also entitled to succeed.

The assessee has its main source of income sole selling agency of Central Distillery and Chemical Works Ltd. It had been its sole selling agent right from the year 1967-68 and every year it has reaped a rich harvest by way of commission. Until 1979-80, it has received about 50 lakhs by way of commission. In this view of things a sole selling agent has always to conform to the wishes of the principal. It cannot choose to reject, much less go against, the will of the principal. The principal after the agreement dated 1st October, 1973 was executed caused a modification of the agreement exparte by sending the letter dated 30th October, 1973. The sole selling agent could not even protest. There was always the Demolies sword in the shape of clause 18 hanging under which by one month's notice the sole selling agency could be terminated. Acting on the basis of the letter dated 30-10-1973 the principal debited the account of the assessee with the irrecoverable amount and reduced his credit from commission by its letter dated 16th May, 1974. The relevant portion is reproduced:-

“We are also debiting the entire amount due from M/S Nagaland Liquor Stores to your account and the necessary debit advice will be forwarded to you in due course.....”

Though as many as five questions have been proposed, however, in sum total the issue remains as to whether assessee is entitled to

deduction of Rs. 4,15,944/- as a business loss on account of amount irrecoverable from M/S Nagaland Liquor Store?

In the present case, it is not in dispute that the assessee was working as sole-selling agent of the principal. It has also come on record that for carrying out its obligation as a sole-selling agent, commission was being paid to it by the principal. To earn commission, the assessee had to carry out certain activities and share certain risk, obligation and responsibility. In the present case, it was agreed upon between the parties by way of communication that the recovery of outstanding dues on account of supply of liquor to parties through the agency of the assessee shall be sole responsibility of the assessee for which he was being paid commission. An agreement can be entered into or extended/modified by way of exchange of letter/communication as well. In the present case, there being valid agreement between the parties, the assessee having agreed to share the responsibility of bad debts on account of non recovery of the amount of liquor supplied through his agency as one of the obligation in lieu of commission being earned by him and that bad debts having been incurred on account of non recovery of such dues from the subsequent buyers, it cannot be said that same does not relate to the business of the assessee. Accordingly, we answer the question against the revenue and in favour of the assessee.

The reference is disposed of, accordingly.

(Rajesh Bindal)
Judge

March 26, 2007
Pka

(M.M.Kumar)
Judge